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Supreme Court of the United States

OCTOBER TERM - 1955

No. 445

NATIONAL SURETY CORPORATION v. THE UNITED STATES. THE FIRST NATIONAL BANK IN HOUSTON, THIRD PARTY DEFENDANT

FIDELITY AND DEPOSIT COMPANY OF MARYLAND v. THE UNITED STATES. THE FIRST NATIONAL BANK IN HOUSTON, INTERVENOR

PETITION FOR WRIT OF CERTIORARI
To The United States Court of Claims
By First National Bank in Houston

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To The Honorable Supreme Court of the United States:

The Petitioner, First National Bank in Houston, respectfully presents this petition for a writ of certiorari to the United States Court of Claims.

a. Opinion of the United States Court of Claims, cited in —Fed. Supp.— appended hereto, and also Opinion of said Court in John A. Hadden, as Trustee in Bankruptcy of Manufacturers Trading Corporation

and Manufacturers Discount Corporation v. The United States, Condenser Service & Engineering Co., Inc., et al., Intervenors, decided on same day and referred to by both the majority and minority of the Court, in the pertinent case, cited in 132 Fed. Supp. 202.

b. The jurisdiction of this Court is invoked upon the following grounds:

(i) The judgment of the United States Court of Claims, sought to be reviewed herein, was made and entered on July 12, 1955.

(ii) The opinion of the majority of the Court is in direct conflict with the opinions of this Court in Central Bank v. United States, 345 U.S. 639, 646, and Martin v. National Surety Co., et al., 300 U.S. 588; and is directly contrary to the holdings of United States Court of Appeals for the Fifth Circuit in Coconut Grove Exchange Bank v. New Amsterdam Casualty Co., 149 Fed. 2d 73, and General Casualty Co. of America v. Second National Bank of Houston, 178 Fed. 2d 679, and contrary to the view expressed by The United States Court of Appeals for the Sixth Circuit in United States v. Hadden, et al., 192 Fed. 2d 327, 329. Further, it is inconsistent with its own opinions in Waxman v. United States, 112 Fed. Supp. 570, 588, and Central Nat. Bank of Richmond, Va. v. United States, 91 Fed. Supp. 738, 740.

(iii) Chapter 81, Title 28, Section 1255, U. S. C. A. which provides: "Cases in the Court of Claims

may be reviewed by the Supreme Court by the following methods:

(1) By writ of certiorari granted on petition of the United States or the claimant."

3. Question presented for review: Whether claims of sureties, based upon assignment provisions in contractor's applications for bonds, are prior and superior to claim of First National Bank in Houston, resting upon assignment to it, duly executed by contractor, pursuant to provisions of Assignment of Claims Act of 1940, (31 U.S.C.A., Sec. 203, 54 Stat. 1029) written notice of same having been duly filed by assignee in accordance with its provisions, as security for money advanced by said assignee to the contractor?

(i) The majority opinion of the United States Court of Claims in Royal Indemnity Co. v. The United States, 117 Ct. Cls. 736 (93 Fed. Supp. 891) and the case at bar, having by interpretation and application frustrated and nullified the intent and purpose of Congress in the enactment of the Assignment of Claims Act of 1940, the question presented is of grave public interest, affecting national defense and security, impelling this Court to resolve the same.

d. Statute involved in the case: Assignment of Claims Act of 1940, as amended, 31 U. S. C. A., Section 203, 54 Stat. 1029, 65 Stat. 41, copy of which is appended hereto.

e. A concise statement of the case containing the facts material to the consideration of the questions presented and involved herein:

This is a case where the National Surety Corporation, the Fidelity and Deposit Company of Maryland, and the First National Bank in Houston assert claim to the unpaid balances of two contracts entered into by and between Thomas Bryan and Associates, Inc., and The United States of America through the United States Atomic Energy Commission, viz:

> Contract No. TA-16, Project D, Los Alamos, New Mexico, known as Contract No. AT (29-1)-994, for the construction of Group 138 Buildings and Facilities, executed September 1, 1950, and to secure the performance of which and payment of labor and material costs, the plaintiff, National Surety Corporation, executed its bonds with the contractor, Thomas Bryan and Associates, Inc., as principal, and itself as surety, claiming the unpaid balance of said contract; and
>
> Contract in Area TA-3, Los Alamos, New Mexico, known as Contract No. AT (29-1)- 838, for the construction of steam and electric plant, executed November 29, 1949, and to secure the performance of which and payment of labor and material costs the plaintiff, Fidelity and Deposit Company of Maryland, executed its bonds with the contractor, Thomas Bryan and Associates, Inc., as principal, and itself as surety, claiming the unpaid balance of said contract; and

The First National Bank in Houston, Texas, as assignee of the contractor, Thomas Bryan and Associates, Inc., claims the unpaid balances of both of the afore-mentioned contracts under (a) Notice of Assignment of Accounts, executed by Thomas Bryan and Associates, Inc. on January 30, 1950, pursuant to Art. 260-1, Texas Civil Statutes, duly filed of record in the office of the County Clerk of Harris County, Texas, pursuant to the provisions of said law on said date; and (b) assignments executed by said Thomas

Bryan and Associates, Inc. on January 21, 1951, pursuant to the Assignment of Claims Act of 1940 (Tit. 31, Sec. 203 U.S.C.A.) and to the provisions of Art. 24(a)(b) (Tr. Stip. pp. 115-116; 166-167) of the afore-mentioned contracts, due notices of which assignments were given as required by said Act and contract provision to all parties therein provided, including the aforesaid surety companies.

That subsequent to the default by Thomas Bryan and Associates, Inc. in the completion of said contracts, the surety companies abandoned said contracts and they were completed by The United States of America (Tr. Stip., pp. 139, 142).

That pursuant to a compromise settlement and stipulation entered with the defendant, The United States of America, by all of said parties, the said defendant is now in the position of a stakeholder only and, as such, is holding an unpaid balance in the sum of $100,918.34 of the afore-mentioned Contract No. AT (29-1)-994, and an unpaid balance in the sum of $65,241.61 of the afore-mentioned Contract No. AT (29-1)-838, subject to the order and judgment of this Court, after deducting an offset by the defendant for taxes in the sum of $45,429.58 apportioned between the two contracts. (Tr. Stip. p. 173, par. 4)

Amplification of Reasons Relied on for Allowance of Writ

a. The question presented has arisen before the United States Court of Claims upon several occasions since Congress enacted the Claims Act of 1940. In the *Royal Indemnity Co.* case, supra, the Court divided three and two; the majority of the Court, in Opinion written by the late Judge Howell, Judges Whitaker and Littleton concurring,

holding Surety had prior and superior right; while Judge Madden wrote a strong dissent, with Jones, Chief Judge, concurring, expressly in agreement with holding of the United States Court of Appeals for the Fifth Circuit in *Coconut Grove Exchange Bank,* supra, and *General Casualty Co.*, supra, cases. The question was squarely presented to that Court in the case at bar. Here the majority opinion is written by Judge Whitaker, and Judges Madden and Littleton concurring, holding Sureties have first and superior right, while Judge Laramore wrote a strong dissenting opinion, with Jones, Chief Judge, concurring. (Dissenting opinion appearing in the *John A. Hadden, Trustee,* case, decided on same day, and which is appended hereto.) Then, too, the question is raised in the *John A. Hadden, Trustee,* case, supra, and in that case Judge Madden wrote the majority opinion with Judge Whitaker, Littleton, and Jones, Chief Judge, concurring, while Judge Laramore wrote the dissenting opinion referred to in case at bar.

These decisions of the Court of Claims create a confusing and unsatisfactory situation, as to the pertinent question, to say the least, and injurious to public interest in that it has set at naught an Act of Congress, the intent and purpose of which is to aid in the national defense. By its decisions, the Court has made that Act of Congress "a snare and a delusion, a trap for the unwary". It remains for this Court to set it aright.

b. First National Bank in Houston made various loans to and advanced funds to the contractor, Thomas Bryan and Associates, Inc., between January 30, 1950 and February 23, 1951, and to secure repayment of funds so loaned and advanced the said contractor executed assignment of Contract No. AT (29-1)-994 and Contract No. AT (29-1)-838 under and pursuant to the Assignment of Claims Act

of 1940, as amended (Tit. 31, 203, U.S.C.A.), notice of which was given to defendant, The United States of America, United States Atomic Energy Commission, and to all other parties, including the plaintiff surety companies, as required by the said Assignment of Claims Act and also in accordance with the provisions of Art. 24 (Tr. Stip., pp. 115, 166) of each of said contracts.

This assignment to the bank is the only legal and valid assignment in the record of this case. The said Assignment of Claims Act, Sec. 203, of Tit. 31, U.S.C.A., expressly excepts a bank from the prohibition against assignments of claims against the United States. It does not except surety companies. The plaintiffs, being surety companies, do not, therefore, have a valid, legal assignment of the unpaid balances of the afore-mentioned contracts. (*Royal Indemnity Co. v. The United States*, 93 Fed. Supp. 891, 894, Ct. of Cls., 1950.)

The record here is clear that the bank made the loans to and advanced the funds to the contractor to assist and enable it to carry on and perform its contracts with the defendant. It has been frequently stated by the courts that this was the purpose of Congress in the enactment of the Assignment of Claims Act of 1940, as amended.

In *Central Bank v. United States*, 345 U.S. 639, 646, where it was urged "that the Act should be construed so as to protect the United States", this Court said: "The short answer to this is that the Act should be construed so as to carry out the purpose of Congress to encourage the private financing of government contracts."

In *General Casualty Co. v. The Second National Bank of Houston*, 178 Fed. 2d 679, 680 (5th Cir., 1949) the Court stated:

> "The original heading of the 1940 amendment of the federal anti-assignment act was as follows: 'To assist in the national-defense program by amending sections 3477 and 3737 of the Revised Statutes to permit the assignment of claims under public contracts.' 54 Stat. 1029. The evident purpose of the legislation was to make it possible for contractors to pledge to a bank, as collateral security, their claims against the Government in order to enable them to borrow money to do the work required by the contract. Pages 12, 557, Part II, Vol. 86, Cong. Record; 31 U.S.C.A. sec. 203, as amended. See also: Prairie State Bank of Chicago v. United States, 164 U.S. 227, 17 S. Ct. 142, 41 L. Ed. 412; Martin v. National Surety Co., 300 U.S. 588, 57 S. Ct. 531, 81 L. Ed. 822; Kane v. First National Bank, 5 Cir., 56 F. 2d 534, 85 A.L.R. 362; Third National Bank of Miami v. Detroit Fidelity and Surety Co., 5 Cir., 65 F. 2d 548; Town of River Junction v. Maryland Casualty Co., 5 Cir., 110 F. 2d 278; Id., 5 Cir., 133 F. 2d 57; Coconut Grove Exchange Bank v. New Amsterdam Casualty Co., 5 Cir., 149 F. 2d 73."

And in *Waxman v. The United States,* 112 Fed. Supp. 570, 588 (Ct. Cls., 1953) the Court pointed out:

> "That Act was amended to make it easier for government contractors to secure financing for carrying out obligations to the Government to the end that government contracts might be speedily and effectively performed. U. S. v. Hadden, 6 Cir., 192 F. 2d 327, General Casualty Co. of America v. Second National Bank of Houston, 5 Cir., 178 F. 2d 679, Royal Indemnity Co. v. United States, 93 F. Supp. 891, 117 Ct. Cl. 736; Central National Bank of Richmond v. United States, 91 F. Supp. 738, 117 Ct. Cl. 389."

Therefore, to deny the bank its right to the unpaid balances of the pertinent contracts is to nullify the purpose and

intent of Congress and constitutes a usurpation of the exclusive function of that legislative body. In the dissenting opinion in the *Royal Indemnity Co. v. United States*, case, supra, it is pointed out that the denial of the claim of the bank under the Assignment of Claims Act is a "substantial frustration of the purpose of said Act."

The situation in *General Casualty Co. v. The Second National Bank of Houston*, supra, was similar, if not parallel, to that of the instant case. There the contractor defaulted and the Government contracted with others to finish the work and the surety company was required under its bonds to pay certain laborer's and materialmen's claims, for which it sought reimbursement out of the unpaid balance of the contract. The trial court adjudged the assignments of the bank superior to rights asserted by the surety company and followed the rule laid down in *Grove Exchange Bank v. New Amsterdam Casualty Co.*, 149 Fed. 2d 73 (5 Cir., 1945). On appeal, the Circuit Court of Appeals affirmed the decision of the lower court and pointed out:

> "Under its assignments, the bank was entitled to the full amount of progress payments due the contractor immediately prior to the latter's default, not to exceed the amount of indebtedness due the bank. The surety was entitled to demand that the sum of the retained percentages withheld by the owner be applied to debts due for labor and material, which the contractor had failed to pay, but there is nothing in the record to indicate that this amount or any portion thereof is a component part of the funds in controversy. The United States was entitled to use the balance of the contract price, including these funds, to complete the contract, which it did; * * *"

And that is the situation here. There is no evidence that the unpaid balances in possession of the United States Gov-

ernment, or any portion thereof, constituted the retained percentages. The implication is well founded that the Government used such funds and portion of the balance of contract price in completing the contracts. Yet, just as in that case, there is here no evidence showing aggregate amount of the retained percentages when the contractor defaulted, nor is there any evidence that the surety companies at that time demanded that the retained percentages be applied to debts for unpaid labor and materials; but on the other hand, the surety companies permitted United States Government to arrange for completion of the work out of retained percentages and other amounts to become due on completion of the contracts. Just as in the *General Casualty Co.* case, supra, there is nothing in the evidence and the Stipulations to contravene the implication that the Government "expended the entire retained percentages in defraying the cost of completing" the contracts.

The rights of the bank and the effect of Section 203 are clearly and irrefutably stated by the Circuit Court of Appeals for the Fifth Circuit, in *Coconut Grove Exchange Bank v. New Amsterdam Casualty Co.*, 149 Fed. 2d 73, 77 (1945), as follows:

> "It is settled by the decisions beyond question that the primary purpose of Section 203, supra, before its amendment, was for the benefit of the Government, and in order to keep it from being embroiled in controversies between the contractors and their assignees and creditors. This is also one of the primary *purposes* of the section as amended, but what is the *effect* of the amendment? Why was there a relinquishment of so many conditions which had theretofore made assignments illegal? Even if, as counsel for both parties concede, the amendment was to facilitate the financing

of contracts in the aid of national defense and to make it so contractors could borrow money from banks and other lending institutions so as to thereby promote the national defense, it still could not now be accurately asserted that the only *effect* was to protect the Government. The amendment made valid that which had theretofore been void and if it were intended not to affect any rights between the parties relating to the validity of such contracts, why did the Act contain the provision that '*Notwithstanding any law to the contrary* governing the validity of assignments any assignment pursuant to this paragraph and the following paragraph shall constitute a valid assignment *for all purposes*'? (Emphasis added.) If an assignment is valid as to the Government but invalid against the Surety and others, could it be said to be 'valid for all purposes'? If the amendment was only for the protection of the Government, why does it provide that the Government could not reduce the assigned claim or set it off by any claim that it has against such an assignor? In addition to protecting the Government, which was the prime purpose of the section before its amendment, as construed in Martin v. National Surety Co., 300 U.S. 588, 57 S. Ct. 531, 81 L. Ed. 822, the amendment of 1940 had the incidental effect of protecting that assignee who filed his assignment and gave notice under the provisions of the statute. Thereafter no other assignment would be effective and all the proceeds would be paid to the one assignee who had complied with the law, provided that assignee were a 'bank, trust company, or other financing institution, including any Federal lending agency'. An assignment made before 'the issuing of a warrant for the payment thereof' to a surety company, which is neither a bank, trust company financing institution or Federal lending agency, is still void and was not made valid by the amendment. We cannot escape the conclusion that the rights of the surety were incidentally affected."

In his dissenting opinion in the *Royal Indemnity Co.* case, supra, Judge Madden (concurred in by Chief Judge Jones) stated that his dissent was "in substantial agreement with the decision in *Coconut Grove Exchange Bank v. New Amsterdam Casualty Co.*, supra."

The Court, in *Coconut Grove Exchange Bank* case, supra, further pointed out that:

> "* * * no superior equity in the Surety will appear unless it shows that the money lent by the Bank was diverted, or used for purposes outside the contract, for if the money lent was applied to the payment of labor and materials used in the contract, thereby discharging obligations for which the Surety would otherwise have been liable, the Surety was in no wise injured by the transaction. It cannot have its liability discharged with the Bank's money and then recover from the Bank money equivalent to that so used for its benefit by its principal. It is fundamental that one seeking in equity to recover money from another must allege and prove injury—not benefit.
>
> "We hold, therefore, that the 1940 amendment of Section 203, while being primarily for the protection of the United States and not for the regulation of the equities of the claimants, as between themselves, nevertheless, did incidentally affect the rights between the assignee of contractor and the surety so as to make assignments to a bank from a contractor for the purposes of the contract valid and the possession by the assignee bank of proceeds of the contract lawful. The $12,220.29 came into the possession of the Bank lawfully by virtue of the only valid assignment that was, or could have been, made under the statute, and anyone seeking to recover any portion of such money had the usual burden of proof. Moreover, to the extent that the money lent by the Bank to the Contractor was used to pay subcontractors or others furnishing labor and materials used

in the performance of the contract, the Surety was not injured, and in the absence of allegations and proof by the Surety Company of a wrongful diversion of funds, it failed to sustain the equitable right which it claims for the recovery of the monies repaid to the Bank."

In the instant case, there is no evidence in the Stipulations, or otherwise, to show that the money lent by the bank was diverted or used for other purposes outside the contracts. On the other hand, the record points to a contrary conclusion. Both contracts were assigned to the bank and the record shows assignment to the bank of invoices of monies due on one of the contracts to the bank (Tr. Stip., p. 113, par. 17), which indicates, at least impliedly, that the money was used directly in the furtherance of the work of said contracts.

WHEREFORE, your petitioner prays that writ of certiorari to the United States Court of Claims be allowed and that this Court review the decision of that Court made and entered herein.

Respectfully submitted,

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